

December 8, 2004

The Honorable Erie County Legislature
25 Delaware Avenue
Buffalo, New York 14202

Honorable Joel A. Giambra
Erie County Executive
95 Franklin Street
Buffalo, New York 14202

Dear Honorable Members and County Executive Giambra:

I am pleased to advise you that we have completed the 2000 year-end closing. As the County's independently elected Comptroller and Chief Fiscal Officer, it is my responsibility to provide you with full disclosure of the County's fiscal condition. In meeting that responsibility, I offer the following overview and selected unaudited financial statements (see Attachment A).

OVERVIEW OF 2000 YEAR END CLOSING

The 2000 General Fund surplus, which is reported as Undesignated Fund Balance in the County's unaudited financial statements, is \$6,813,036 and is attributable to the following factors:

I. Designations	\$(44,244,047)
II. Net 2000 Favorable Budget Variances	38,889,077
II. Net Reduction of Prior Year Reserves & Liabilities	<u>12,168,006</u>
Reported General Fund Surplus	<u>\$ 6,813,036</u>

The following is an explanation of the items presented in the preceding table:

I. DESIGNATIONS

Discretionary designations, for purposes not included in the Adopted 2000 Budget, were established in 2000 as follows:

For Erie County Medical Center (Administrative Directive)	\$24,800,000
For future bonded debt (2001 Budget, Resolution #2, pages R1-2)	10,000,000
For use in the 2001 Budget (2001 Budget, P. 191)	8,786,609
For Lackawanna Senior Housing (Administrative Directive)	337,847
For Buffalo Schools (Resolution Intro. 4-13)	253,000
For the County fleet (Administrative Directive)	<u>66,591</u>
Total	<u>\$44,244,047</u>

As of December 31, 2000 the total of all General Fund fund balance designations, including the above, is \$149,549,056, (see Attachment B).

Based on a combination of Generally Accepted Accounting Principles (GAAP), the Omnibus Resolution, administrative directives and legislative actions, the Comptroller's Office has reported designations of fund balance for various purposes in the financial statements. These designations of fund balance have a direct impact on the amount of Undesignated Fund Balance to be reported and, therefore, on the size of the real property tax levy.

In years prior to 1999, multi-million dollar expenditures and designations of fund balance were made under the authority of the Omnibus Resolution. I frequently warned the County Legislature of the fiscal consequences of granting the administration unrestricted authority afforded by the Omnibus Resolution. In a letter to the County Legislature dated April 19, 1999 I wrote: "The delegation of legislative authority to the administration allows for multi-million dollar designations of the County's funds for purposes that the people, through their representatives, may not approve of. The administration, pursuant to the Omnibus Resolution, arbitrarily determines the need for various reserves and designations, which impact the amount of taxes that must be levied to balance subsequent budgets. The authorities and responsibilities as outlined in the Erie County Charter and Administrative Code should not be overruled by a single (Omnibus) resolution of the Legislature".

Although the Omnibus Resolution has now been rescinded, designations continue to be made but in the absence of formal written policy. I have consistently criticized the delegation of authority by the Omnibus Resolution and I am similarly opposed to the unstructured establishment of fund balance designations without formal written policy.

GAAP provides little direction or authoritative guidance concerning designations, although they are acknowledged, as follows:

“Fund balance designations may be established to indicate tentative plans for financial resource utilization in a future period, such as for general contingencies or for equipment replacement. Such designations reflect tentative managerial plans or intent and should be clearly distinguished from reserves. Such plans or intent are subject to change and may never be legally authorized or result in expenditures. Designated portions of fund balance represent financial resources available to finance expenditures other than those tentatively planned. Designations should be reported as part of the unreserved fund balance Designated for..., or disclosed parenthetically or in the notes to the financial statements.” (NCGAS 1, ¶120)

I recommend that the administration, in coordination with the County Attorney’s Office, establish a formal written policy on designations, minimally specifying the types of designations allowed, the required approvals for establishment, and pre-requisites for appropriation.

I have regularly criticized balancing annual budgets with significant amounts of windfalls and prior year reserves and/or designations. Rather than rely on reserves and/or designations, recurring expenditures should be financed from recurring revenues. The following schedule (expressed in thousands) presents the amount of reserves and/or designations used to balance the budgets of the General and Debt Service Funds since 1989:

<u>Budget Year</u>	<u>Two-year Rule Undesignated Fund Balance</u>	<u>Current Year Variance & Other Prior-Year Resources</u>	<u>Total</u>
1989	\$ 3,805	\$ 2,089	\$ 5,894
1990	294	3,367	3,661
1991	2,341	8,137	10,478
1992	3,771	15,168	18,939
1993	267	11,217	11,484
1994	3,001	21,281	24,282
1995	973	16,392	17,365
1996	2,868	38,911	41,779
1997	4,592	23,681	28,273
1998	6,665	34,105	40,770
1999	7,604	58,001	65,605
2000	5,882	58,860	64,742
2001	14,961	58,247	73,208

The specific sources of \$73.2 million in current and prior-years resources to fund 2001 appropriations are:

\$14,961,128	1999 Fund Balance, unreserved, undesignated.
36,511,297	Partial usage of 1999 Designation for Structural Budget Repair.
8,786,609	Cancellation of various General Fund reserves.
3,135,269	Various Debt Service Fund reserves.
<u>9,813,541</u>	Various reappropriations authorized by 2000 Budget Resolutions.
<u>\$73,207,844</u>	Total current and prior-year resources utilized in the 2001 Budget.

I repeat my recommendations from previous years that recurring expenditures be financed from recurring revenues and that the level of reliance on reserves and fund balances be reduced.

II. NET 2000 FAVORABLE BUDGET VARIANCES

During the course of every fiscal year, actual operations differ from the adopted budget in many ways. Some actual amounts are under budget, some over budget. The summary below shows the three major components of the net favorable budget variance for 2000 of \$38,889,077.

Social Service Programs	\$19,921,205
Countywide Accounts	19,859,448
Departmental	<u>(891,576)</u>
Net 2000 Favorable Budget Variances	<u>\$38,889,077</u>

A detailed breakdown of the three major components of the net favorable variance for 2000 of \$38,889,077 follows:

Social Service programs:

Administration and Title XX	\$ 6,257,733
Medicaid	3,168,893
Temporary Assistance to Needy Families	2,918,415
Child Welfare Services	2,109,116
Medicaid Management Information Systems	1,891,463
Safety Net	643,453
Other Social Service Programs	<u>2,932,132</u>
Total 2000 DSS Favorable Variances	<u>\$19,921,205</u>

Countywide Accounts:

Sales Tax Revenue	\$13,212,181
Property Tax Accounts	11,451,640
Prison Aid-U.S. Marshals Service	1,000,000
Tobacco legal cost reimbursement	543,926
Tobacco revenue shortfall	(2,246,581)
ECMC subsidy increase	(1,919,926)
Flood damage-Pay as you go capital	(1,023,500)
NFTA share of Sales Tax	(796,139)
Reserve for Lackawanna Sr. Housing loan	<u>(362,153)</u>
Net 2000 Countywide Favorable Variances	<u>\$19,859,448</u>

Departmental:

Holding Center revenue from other governments	\$ 931,455
Various programs, under \$500,000 each	2,529,062
Holding Center payroll	(2,289,105)
Payroll, all other departments	<u>(2,062,988)</u>
Net 2000 Departmental Unfavorable Variance	<u>\$ (891,576)</u>
Total Net 2000 Favorable Budget Variances	<u>\$38,889,077</u>

III. NET REDUCTION OF PRIOR YEAR RESERVES AND LIABILITIES

The following is a brief description of the Net Reduction of \$12,168,006 in reserves and liabilities in 2000:

Cancel designation for potential Social Services losses relating to the Federal Administration for Children & Family claims audit. Notification was received in 2000 that Erie County was not subject to any losses due to audit adjustments.	\$4,786,609
1998 encumbrances for Aud Demolition Assistance and for Cobblestone District Development, each at \$2,000,000, were cancelled in 2000.	4,000,000
A 1999 designation for ECC Programs was cancelled. The ECC programs were actually carried out in 2000 through the Capital budget.	1,700,000
Cancellation of excess Health Department Children with Special Needs liability. This liability was reduced to the amount expected to be expended in future years per program regulations.	1,289,150
Increase in the Reserve for Advances to ECMC account.	(116,868)
Cancellation of excess 1999 Aid to Indigent Prisoner's liability. The 1999 Agency audited financials revealed an overstated County liability.	<u>509,115</u>
Net 2000 Reduction of Prior Year Reserves and Liabilities	<u>\$12,168,006</u>

TOTAL FUND BALANCE

The \$6,813,036 surplus is only one of several components of Total Fund Balance for the General Fund. The total balance at December 31, 2000 is \$202,041,408, which is \$13,199,406 more than a year ago, as shown below:

<u>FUND BALANCES</u>	<u>2000</u>	<u>1999</u>	<u>Increase (Decrease)</u>
Reserved for Encumbrances	\$19,994,915	\$14,284,450	\$5,710,465
Reserved for Advances to ECMC	10,813,043	10,696,175	116,868
Reserved for Retirement	14,509,205	16,749,652	(2,240,447)
Reserved for Long Term Lackawanna Senior Housing Loan	362,153	-	362,153
Designated for use in the next year's Budget	60,259,034	32,989,076	27,269,958
Designated for Contingencies	3,737,003	4,182,587	(445,584)
Designated for Aid to Localities	6,076,538	8,326,163	(2,249,625)
Designated for Social Services Losses	3,326,667	8,113,276	(4,786,609)
Designated for Grant Programs	8,903,673	8,539,495	364,178
Designated for Structural Budget Repair	31,788,703	68,300,000	(36,511,297)
Designated for ECC	-	1,700,000	(1,700,000)
Designated for ECMC	24,800,000	-	24,800,000
Designated for Bonded Debt	10,000,000	-	10,000,000
Designated for Lackawanna Senior Housing	337,847	-	337,847
Designated for Buffalo Schools	253,000	-	253,000
Designated for County Fleet	66,591	-	66,591
Total Reserves and Designations	<u>\$195,228,372</u>	<u>\$173,880,874</u>	<u>\$21,347,498</u>
Undesignated (Surplus)	<u>6,813,036</u>	<u>14,961,128</u>	<u>(8,148,092)</u>
Total Unaudited General Fund Balance	<u>\$202,041,408</u>	<u>\$188,842,002</u>	<u>\$13,199,406</u>

EXPECTATIONS FOR 2001 AND BEYOND

Erie County taxpayers have enjoyed a 31.2% tax cut over the past two years (see Appendix I).

As shown in Appendices II and III, the tax levy was reduced from 1999 to 2000 by nearly \$40 million and from 2000 to 2001 by over \$29 million. This contrasts dramatically with the tax levy during the Gorski administration, when property taxes increased nearly 70% or by over \$91 million from 1988 to 1999 (see Appendix IV).

However, more discipline is needed in the budget development and budget monitoring processes to assure the County is not forced to return to the years of annual property tax increases.

There are other factors that may impact Erie County's finances in the near term. The New York State and Local Retirement Systems (NYSERS) have recently advised us to expect higher retirement costs in 2001. The higher costs are a direct result of NYSERS investment losses realized when the world's stock markets underwent corrections from record levels achieved through early 2000. Erie County's increased cost of retirement contributions is estimated at \$5 million.

The economic slowdown we are currently experiencing will make operational gains more difficult to achieve in 2001, especially in economically sensitive areas such as sales tax and investment income. The uncertainty of the full financial impact of this economic slowdown makes it important for Erie County to be cautious.

As we complete the financial closing of 2000, I am particularly concerned with two areas:

- ECMC – In a letter dated May 4, 2001, I made you aware of my growing concern over the ever-increasing financial burden being placed on the County by the deteriorating fiscal condition of the Erie County Medical Center (ECMC). At my urging, the administration has established a designation of fund balance for ECMC in the amount of \$24.8 million. This should be sufficient to absorb any near term problems at ECMC. I will continue to monitor the financial condition of ECMC and recommend that you arrange to meet with ECMC financial management to review any concerns that you may have.
- NON-RECURRING REVENUES TO BALANCE THE BUDGET – The 2001 Adopted Budget is balanced in part by the use of \$73.2 million in largely non-recurring revenues. Continued budgetary reliance on reserves and/or designations in such significant amounts will soon deplete the Fund Balance unless spending is also cut back substantially or new revenue sources are found. As I have stated previously, recurring expenditures need to be financed from recurring revenues.

As we look ahead, I urge that:

- More discipline be employed in budget development and budget monitoring.
- The administration in coordination with the County Attorney establish a formal written policy on designations.
- Recurring expenditures be financed by recurring revenues.

If you have any questions, please do not hesitate to contact me at 858-8404.

Very truly yours,

NANCY A. NAPLES
Erie County Comptroller